United States
COURT OF APPEALS
for the Ninth Circuit

STATE FARM MUTUAL AUTOMOBILE INSURANCE COMPANY, a corporation,

Appellant,

v.

DONALD L. BREWER, administrator of the estate of William Ira Pate, deceased,

Appellee.

APPELLANT'S BRIEF

Appeal from the United States District Court for the District of Oregon

HONORABLE BRUCE R. THOMPSON, Judge

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JURISDICTIONAL STATEMENT

The jurisdiction of the United States District Court to hear this cause is based upon an amount in controversy in excess of $10,000.00, exclusive of interest and costs, between citizens of different states. (Act of July 25, 1958, 72 Stat. 415, Amending 28 U.S.C.A. § 1331 and 1332) (R. 1). The jurisdiction of this Court to review the District Court's decision is based

upon § 1291 of Title 28, United States Code, this appeal having been taken from a final judgment entered on November 7, 1966 (R. 153).

STATEMENT OF THE CASE

Appellee commenced this action in the District Court for the District of Oregon, seeking a judgment against appellant in the amount of $31,979.38 plus interest (R. 6). Appellee alleged that he had been appointed administrator of the estate of William Ira Pate, deceased, who had been insured by appellant for liability for bodily injury and property damage caused by accident arising out of the ownership, maintenance, or use of a motor vehicle. Appellee had been involved in a collision with a motor vehicle operated by the deceased Pate and, as a result of this action, recovered a judgment against Pate in the Circuit Court of the State of Oregon for the County of Multnomah in the amount of $42,141.25.

Appellee alleged that appellant acted in bad faith and violation of its fiduciary duty to the deceased in that it failed to accept appellee's offer to accept $10,000.00 in full settlement of the claim prior to the entry of the judgment in Multnomah County and further, to accept appellee's offer to accept $10,000 in full settlement of the judgment after the entry of the judgment.

After the verdict in the Circuit Court for the State of Oregon, appellant filed a motion to set aside

the verdict and grant a new trial on the basis of newly-discovered evidence (R. 4). This motion was denied by the State Court on May 5, 1964 (R. 4).

On November 7, 1966, the Court below entered its findings of fact and conclusions of law (R. 122-126), in which it found that the appellant had acted in good faith and with due and proper regard of the interests of its insured prior to the verdict in the State Court action. The Court further found that the appellant was careless and negligent and acted in disregard of the interests of its insured in failing to accept appellee's offer to settle within the limit of its policy after the verdict and prior to the Court's ruling on the motion for new trial.

Based upon the findings, the Court below found that the estate of appellant's insured had been damaged by the tortious conduct of appellant in the amount of $31,979.38 and entered judgment (R. 127).

SPECIFICATIONS OF ERRORS

I. The good faith determination by an insurer that its insured will not necessarily be found liable for damages suffered by a claimant is not changed by a jury determination that the insured was negligent.

II. The extent of the damage to the estate of the appellant's insured was only $461.18.

III. Interest, bias, and inconsistency must be considered in evaluating the testimony of a witness.

IV. Attorney's fees are not to be awarded in actions based upon negligence of an insurer in failure to settle a claim against its insured.

SUMMARY OF ARGUMENT

State Farm, the insurer, had, in the State Court action, in good faith, determined that its insured would not necessarily be found liable for the damages suffered by Breuer and consequently refused to settle with the claimant. After trial and a resulting jury verdict and during the pendency of a motion for a new trial, it is asserted that additional offers to settle were made. Appellant, State Farm, should not be required to abandon its position because of a jury determination. To do so would effectively deprive a company of its right of appeal.

The object of compensatory damages is to make the person injured whole. The damages which are the subject of this action are the damages to State Farm's insured, *not* the damages to the claimant, Breuer. Since it is established that the insured's estate was limited to $461.18, that should be the total amount of damages involved.

The sole source of the testimony concerning the communication of offers of settlement subsequent to the jury's verdict in the state court is the testimony of the attorneys involved; and this testimony is diametrically opposed. It is necessary to examine the credibility of the witnesses involved. On the basis of interest, bias, and inconsistency, the testimony of the

attorney for the claimant is of less weight and force than the testimony of the defendant's counsel.

ARGUMENT I.

A. The appellant as an insurer, having, in good faith without negligence, determined that its insured would not necessarily be found liable for the damages suffered by the claimant should not be required to abandon that position in the face of a jury verdict in excess of the limit the defendant has contracted to pay in the event of its insured's liability.

An insurance company which has defended and negotiated in good faith on behalf of its insured should not be required, after the rendition of a verdict in excess of its policy limits, to accept such an offer. The duty, under its contract, of the insurer is to protect its financial interest and that of its insured. To require the insurer to accept any offer within the limits of the contract after a trial verdict in excess of those limits would have the effect of denying the company its right to an appeal. *Chancey* v. *New Amsterdam Cas. Co.*, 336 S.W.2d 763. If an insurance company has been determined to have honestly defended its insured interests up to the point of verdict, in the face of such a rule it could retire its obligation by paying that portion of the verdict it was contractually obligated to pay, even though it properly felt there was manifest error in the trial of the case. To impose such a rule would result in a disservice both to the responsibility of the company and its insured. The duty to properly defend should not end at the trial

court level. The effect of such a rule would deprive the insured of the very benefit for which he has paid.

The problem of excess liability has become increasingly important to the automobile insurance companies. This can be attributed to high verdicts and a generally more liberal attitude of the courts in permitting excess recoveries from the insurance companies. Consequently the question of good faith on the part of the insurer becomes of paramount importance. Although many recent cases have been decided on the question of good faith, it is a relatively new area in Oregon. The Oregon Supreme Court has rendered only three decisions on the issue under consideration. Due to the absence of litigation, there is yet to be established in this state a definite standard as to what constitutes good faith or, in the negative, bad faith. This deficiency was recognized by Justice Rossman in his opinion in the case of *Radcliffe* v. *Franklin Nat'l Ins. Co.*, 298 P.2d 1002, where he succinctly stated:

> "Universal recognition that the insurer owes a duty in regard to the settlement of claims and actions has not yielded a rule which clearly defines the duty."

The *Radcliffe* case is the only case which serves to enlighten this jurisdiction on the issue of what constitutes good faith conduct by an insurer in an excess liability case. The *Radcliffe* decision was given additional support by the Oregon Supreme Court in the recent decision of *Kuzmanich* v. *United Fire & Casualty Co.*, 410 P.2d 812.

The *Radcliffe* case, like the instant case, was an action against an automobile liability insurer to recover the amount of a judgment entered against the insured in excess of the policy's coverage. In *Radcliffe*, however, judgment was entered for the defendant on a directed verdict. The court found that if the insurer had exercised due care in its investigation, evidence regarding liability and injuries would have been available which might have led to the acceptance of settlement offers within the policy limits.

In defining the duty of the insurer, the opinion concludes:

> "Negative elements do not meet the demands of good faith. A decision by one who is ignorant of the controlling facts is worthless. Only a decision made by one who exercised due diligence in apprising himself of the material facts is entitled to respect as made in good faith."

Although establishing a stringent standard of liability for insurers in cases involving failure to settle within policy limits, the *Radcliffe* opinion clearly recognizes that the insurer is not obligated to sacrifice its own interest. The quality of consideration to the respective interests of the parties, not sacrifice of the insurer's interest to that of the insured, is the required standard.

> "Plainly, an automobile owner who produces a policy of limited liability insurance understands that the company is in business and that unless it looks after its own interests it cannot expect to survive. The insurer, obviously, has a right to

> give heed to its own interests when it considers settlement offers, but when it does so it must give at least as much attention to those of the insured."

In the context of the *Radcliffe* case, there can be no doubt of the substantiality of the evidence to support the trial court's findings. The lack of due care found in the *Radlcliffe* case in investigating the claim and in apprising the insured of settlement offers is totally lacking in the present case. In further contrast to the *Radcliffe* case, the evidence here discloses a thorough and complete investigation of all facits of the claim underlying the former action. All prospective witnesses who might have contributed information concerning the case were contacted and interviewed, every possible source of relevant information was investigated, and that information obtained was carefully evaluated. The entire record and file of the insurer points to the conclusion that the rejection of settlement offers was based on a well-documented, conscientiously-evaluated mass of facts which provided ample basis for the conclusion that the insurer was not liable upon the claim.

In applying the standards estabilshed by the *Radcliffe* case to the case under consideration, in view of the substantial evidence of appellant's records before the Court, it can be concluded that the appellant insurer has exhibited conduct which has been marked by due care and good faith through the course of this case.

In the *Kuzmanich* case, the Oregon Supreme Court

applied the standard as established by the *Radcliffe* case, where in the opinion the Court held:

> "An insurer owes to its insured the duty of due diligence and good faith. In determining whether to settle claims against the insured, the insurer must act as if it were liable for the entire judgment that might eventually be entered against the insured. In addition, only a decision made by an insurer who exercises due diligence in apprising itself of the material facts is entitled to be considered as made in god faith." *Radcliffe* v. *Franklin Nat'l Ins. Co.*, 298 P.2d 1002.

With this standard established, the Court concluded that there was no element of bad faith on the part of the insurer.

> "It is the court's opinion there was sufficient substantial evidence to sustain the findings of the trial court to the effect that defendant was not negligent and did not exercise bad faith. The investigations made by defendant prior to trial appear to have been adequate and complete." *Kuzmanich* v. *United Fire & Casualty Co.*, supra.

Since the trial court found in applying Oregon law stated above that the appellant had used reasonable care, skill, and diligence prior to the determination of the jury (R. 123), it cannot be said that it failed to do so in refusing to accept an offer within the policy limits thereafter.

B. The appellant's motion for a new trial in the personal injury action filed in the state court proceeding was not perfunctory in nature but was well founded.

The statutes of the State of Oregon provide the grounds upon which a judgment may be set aside and a new trial granted. Such statute provides:

> "17.610. Causes for granting new trial. A former judgment may be set aside and a new trial granted on the motion of the party aggrieved for any of the following causes materially affecting the substantial rights of such party:
>
> "(1) Irregularity in the proceedings of the court, jury or adverse party, or any order of the court, or abuse of discretion, by which such party was prevented from having a fair trial.
>
> "(2) Misconduct of the jury or prevailing party.
>
> "(3) Accident or surprise which ordinary prudence could not have guarded against.
>
> "(4) Newly discovered evidence, material for the party making the application, which he could not with reasonable diligence have discovered and produced at the trial.
>
> "(5) Excessive damages, appearing to have been given under the influence of passion or prejudice.
>
> "(6) Insufficienty of the evidence to justify the verdict or other decision, or that it is against law.
>
> "(7) Error in law occurring at the trial, and excepted to by the party making the application."

One of the grounds upon which the motion for new

trial was based was the use of a false name by the plaintiff in the state court proceedings. The plaintiff in the state court proceedings used the name "Lee D. Breuer" when in fact his true name was "Donald L. Brewer." The use of a false name was obviously a fraud upon the Court and the public. This is further evidenced by Donald L. Brewer having applied with the State of Oregon for a driver's license under the name of Lee D. Breuer when in fact his driver's license under his true name had been suspended for driving violations (Tr. 7-8).

The failure of the plaintiff in the state court proceedings to reveal his true name deprived the appellant's insured of substantial rights in investigation, cross examination, and the right to have the jury consider the use of a false name in determining the credibility to be given to Breuer's testimony.

Such rights were of great importance to appellant's insured in the state court proceedings, as the liability question was doubtful and the jury was required to adopt either the testimony of the plaintiff or that of the defendant.

Based upon the grounds appellant's insured had for his new trial, the appellant herein certainly had the right, without being guilty of bad faith or negligence, to have the motion determined before being compelled to pay its policy limits.

ARGUMENT II

An insured who has had a judgment in excess of policy limits rendered against him has not been injured until such time as he has paid or is shown to have assets subject to the judgment which exceeds the limits of his insurer's contractual obligation.

The crucial question is whether the insured has been harmed. *Harris* v. *Standard Accident and Ins. Co.*, 297 F.2d 627. Damages, either in tort or contract, accrue when the plaintiff has been injured; and the claimant's right in an action against the insurer can rise no higher than the rights of the insured. *Suguros Tepeyac, S.A., Companie Mexicana de Seguros Generales* v. *Bostrom*, 347 F.2d 168. Regardless of whether the duty of the insurer lies in tort or contract, the duty is to respond in damages. It must be borne in mind that these are *not* the damages that have been inflicted *by the insured* but the damages that may have been inflicted *upon the insured.*

> "The purpose of tort damages is to compensate an injured person for the loss suffered and only for that." *Harris* v. *Standard Accident & Ins. Co.*, supra at 627.

Equally in contract:

> "The cardinal purpose of the law of damages is to place the wronged party in as good a position as he would have been in had the other performed his contract." *Stubblefield* v. *Montgomery Ward & Co.*, 96 P.2d 774.

The basis of an action for wrongful failure to set-

tle is the damage to the insured, not the damage to the person the insured may have injured. It is argued that the insured suffers from the excess judgment lodged against him. To say that an insured is damaged thereby alone without his paying or having assets subject to execution on the judgment is to ignore what in fact happens. The impact of the judgment will never reach him or his estate. Had he lived, bankruptcy would have discharged him; and the assets of the decedent's estate are beyond the reach of this judgment creditor. This applies to judgment creditors as well as general and secured creditors. Ultimately the only person who would be compensated by a judgment against the defendant in this action is the person the insured insisted was not entitled to compensation.

Except for the sum of $461.18, the estate of William Pate is wholly insolvent. It is incumbent upon the appellee to show that the estate of William Pate will suffer pecuniary damage by reason of the excess judgment. The excess judgment stands on the same footing as any other non-preferential claim against the estate and under the provisions of Oregon Revised Statute 117.110 can be satisfied only after satisfaction of the preferential items. ORS 117.110 states:

> "Order of payment of charges and claims. The charges and claims against the estate which have been presented and subsequently established by judgment or decree within the first six months after the date of the notice of appointment of the executor of administrator, shall be paid in the fol-

lowing order, and those presented and allowed or established in like manner within each succeeding period of six months thereafter, during the continuance of the administration, in the same manner:

"(1) Funeral charges and expenses of last sickness.

"(2) Taxes of whatever nature due the United States.

"(3) Taxes of whatever nature due the state, or any county or other public corporation therein.

"(4) Debts preferred by the laws of the United States.

"(5) Debts which, at the death of the deceased, were a lien upon his property, or any right or interest therein, according to the priority of their several liens.

"(6) Debts due employes of decedent for wages earned within the last 90 days immediately preceding the death of the decedent.

"(7) The claim of the State Public Welfare Commission for the net amount of public assistance, as defined in ORS 411.010, paid to or for the decedent and the claim of the Oregon State Board of Control for care and maintenance of any decedent who was at a state institution to the extent provided in ORS 179.610 to 179.770.

"(8) All other claims against the estate."

Until the appellee has sustained the burden of showing that after satisfying the claims of preferential creditors as is required by ORS 117.110, there remains funds in the estate by which the estate can suffer pecuniary damage, there can be no damage to

the estate. The contract of insurance is a contract of *indemnity*, and the obligation of the insurer is to make the insured whole. *Hardwick* v. *State Ins. Co.*, 26 Pac. 840.

ARGUMENT III

The Court, when sitting as a trier of fact, must consider the credibility of a witness and must evaluate interest, bias, and inconsistency.

Reluctantly, but necessarily, attention must be drawn to the testimony of Mr. Ryan, the attorney for the plaintiff in the trial court proceeding. Although the appellant is convinced that the arguments presented above should establish that it has acted within the standard of care required of it and has not breached its contract with the insured and neither the insured nor his estate has been damaged by the appellant's conduct, appellant is still required to call to the Court's attention those matters which affect the credibility of Mr. Ryan's testimony.

A. The credibility of a witness in each case must be determined by the trier of fact.

Herein the Court, as a trier of fact, is faced with the difficult and delicate problem of determining which of the two testifying attorneys more accurately recalls the events surrounding the settlement negotiations prior and subsequent to the verdict in the state court. Unpleasant as this task may be, unless the Court rules for the appellant on one of the two preceding arguments, this determination must be made.

B. Inconsistency of testimony.

(1) In the course of the deposition of Mr. Ryan, it was indicated that the offer to settle within the limits was made by way of a telephone conversation. (Pl. Ex. 28, p. 9). In the course of Mr. Ryan's testimony at trial, he indicated that offers of settlement were made in person during an automobile ride.

(2) Plaintiff's Exhibit 20 obviously indicates that counsel for Breuer (Brewer) are aware of the possibility that the defendant insurer might be held liable for failure to settle within the limits of the policy and consequently arranged that offers and demands were made in writing, yet during the period subsequent to the jury verdict they appear to have neglected the establishment of a record of offers despite their contention that defendant might be under a greater duty to accept such an offer.

(3) The testimony of Mr. Samuels, the attorney for the defendant insurer, and the exhibits presented show a consistent pattern of written communication of all offers to his client, the insurer, yet no record, despite extensive discovery procedure, has been produced showing any such communication subsequent to the verdict of the jury.

C. Interest of the witness.

The fact that a witness is the attorney for one of the parties goes to his credibility even though he does not appear in the case as an attorney after he testifies. *In re Comegys Estate*, 284 P.2d 512.

An attorney's credibility is especially affected where his employment is on a contingent fee. *Harrington* v. *Hamberg*, 85 Iowa 272; *Firth* v. *Briarton*, 212 N.W. 805.

It is necessary to call to the Court's attention that the firm of which Mr. Ryan is a member continues to press this action. There is no intention of implying that Mr. Ryan is testifying to facts contrary to his recollection, the rule of interest as affecting credibility is based upon the practical fact that memory is inclined, when in doubt, to follow interest; and it is respectfully urged that this should be borne in mind in evaluating the testimony of the witnesses before the Court.

ARGUMENT IV

Atorneys fees are improperly awarded in an action based upon the negligence of an insurer as they are limited to actions on the contract of insurance between the contracting parties thereto.

The appellee's theory of recovery is based on either the negligence of the appellant or that the appellant, in bad faith, rejected the offer of appellee to settle the claim of appellee for the policy limits and in refusing to pay its policy limits (R. 1-6).

The statutes of the State of Oregon provide for recovery of attorney fees against an insurance company only if suit or action is brought upon the policy of insurance. The statute provides:

"736.325. Recovery of attorney fees in action

on policy. (1) If settlement is not made within six months from the date proof of loss is filed with an insurance company, fraternal benefit society or health care service contractor and a suit or action is brought in any court of this state upon any policy of insurance of any kind or nature, including a policy or certificate issued by a fraternal benefit society as defined in ORS 740.010 and a contract or agreement issued by a health care service contractor as defined in ORS 742.010, and the plaintiff's recovery exceeds the amount of any tender made by the defendant in such suit or action, then the plaintiff, in addition to the amount that he may recover, shall be allowed and shall recover as part of his judgment such sum as the court or jury may adjudge to be reasonable as attorney's fees.

"(2) If attorney fees are allowed as provided in this section and on appeal to the Supreme Court by the defendant the judgment is affirmed, the Supreme Court shall allow to the respondent such additional sum as the court shall adjudge reasonable as attorney fees of the respondent on such appeal."

It is apparent from the complaint filed by the appellee that this is not an action upon the policy of insurance issued by the appellant but is an action sounding in tort, either upon bad faith or negligence.

The distinction between an action upon a contract, such as a policy of insurance, and one founded upon a tort by reason of a relationship established by a contract between the parties has been discussed by the

Court in *Harper* v. *Interstate Brewery Co.*, 120 P.2d 757:

> " 'The *Distinction between a Tort and a Breach of Contract* is broad and clear, in theory. In practice, however, it is not always easy to determine whether a particular act or course of conduct subjects the wrongdoer to an action in tort, or merely to one for a breach of contract. The test to be applied is the nature of the right which has been invaded. If this right was created solely by the agreement of the parties, the plaintiff is limited to an action *ex contractu.* If it was created by law he may sue in tort." Burdick on Torts (4th ed.) Page 46."

67 Harvard Law Review, page 1136.

The action of the appellee is based upon a tort. It is not an action to recover a loss under the policy of insurance. Therefore, appellee is not entitled to attorneys fees. *Zumwalt* v. *Utilities Ins. Co.*, 228 S.W.2d 750.

Respectfully submitted,

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CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit and that, in my opinion, the foregoing brief is in full compliance with those rules.

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Of Attorneys for Appellant